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UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW HAMPSHIRE

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U.S. SECURITIES AND EXCHANGE
COMMISSION

v.

LBRY, INC.

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21-cv-260-PB
July 20, 2022
1:00 p.m.

TRANSCRIPT OF MOTION HEARING
BEFORE THE HONORABLE PAUL J. BARBADORO

APPEARANCES:

For the Plaintiff:

Marc Jonathan Jones, Esq.
Amy Burkart, Esq.
Securities and Exchange Commission

For the Defendant:

Keith Miller, Esq.
Emily Drinkwater, Esq.
Perkins Coie, LLP

Timothy John McLaughlin, Esq.
Shaheen & Gordon

Court Reporter:

Susan M. Bateman, RPR, CRR
Official Court Reporter
United States District Court
55 Pleasant Street
Concord, NH 03301
(603) 225-1453

P R O C E E D I N G S

THE CLERK: This Court is in session and has for consideration a motion hearing in civil matter 21-cv-260-PB, U.S. Securities and Exchange Commission versus LBRY, Inc.

THE COURT: All right. First, I would like to just take a minute and thank the parties for their briefs and compliment you. I mean, I really feel the briefs are very well done and were quite helpful to me, the briefs on both sides.

Let me explain to you how I would like to proceed. The SEC has filed a motion to strike a limited supplemental disclosure by one of the defendant's experts. That motion is serious, and I recognize there's a real potential for unfair prejudice if I were to allow the motion to be -- excuse me -- allow the supplemental disclosure to be included in the materials that I would consider in ruling on the parties' cross-motions for summary judgment, but I think that LBRY has proposed the outlines of the solution, at least an interim solution to that problem.

As I understand LBRY's disclosure, response to the motion to strike, you're saying, hey, Judge, if there's a -- if you have a significant concern of unfair prejudice, just don't include the supplemental disclosure on these briefs and we'll live to fight another day about whether the disclosure can be used in some subsequent proceeding like a trial.

1 That would address my most -- my most immediate
2 concern is I think it would be unfairly prejudicial to the SEC
3 to allow you to just add to the record on summary judgment
4 something like that so late in the process under these
5 circumstances.

6 But I understand your argument that if we get
7 beyond this, the prejudice is obviously lessened and there are
8 other remedies that I might use, like reopen discovery, allow
9 supplemental depositions, things like that, and that's at
10 least a viable alternative.

11 So it would seem to me the best thing to do would
12 be to simply proceed without consideration of the supplemental
13 disclosure in ruling on the parties' cross-motions because as
14 LBRY has pointed out, you don't rely extensively on the
15 supplemental disclosure. You argue that you can prevail
16 regardless of whether I can consider it, and you appear to be
17 willing to allow me to rule on the motions without considering
18 it.

19 And since there's a danger of unfair prejudice it's
20 very prevalent to me if I were to consider it now, I would
21 propose that we simply agree that it will not be considered on
22 these motions. I will rule on these motions as if it had not
23 been filed and deny the motion without -- deny the motion to
24 strike without prejudice to the SEC's right to renew it.
25 Subsequently, in light of that agreement, the immediate

1 concern for unfair prejudice could be in my mind
2 satisfactorily addressed.

3 So let me first ask for the LBRY's -- whether I've
4 read enough into your response that what I'm suggesting to you
5 would be acceptable to you. Would you let me know whether
6 that is?

7 MR. MILLER: Yes, your Honor. That's agreeable and
8 acceptable.

9 THE COURT: All right.

10 So I understand your argument. It's fully
11 preserved with respect to supplemental if the case survives
12 summary judgment.

13 I don't see how it's unfair to you in any way given
14 their agreement that I'll act as if it doesn't exist for
15 purposes of these motions. So I would assume that's
16 acceptable to the SEC.

17 MR. JONES: It is, of course, your Honor, more than
18 fair. I would ask -- we would preserve that if in fact we
19 proceed beyond this.

20 The other thing is that the amended report concedes
21 substantial methodological and factual errors that are in the
22 original report. So I would ask your Honor to at least take
23 that into account if your Honor is still going to consider the
24 original report.

25 THE COURT: It's sort of in for a penny, in for a

1 pound kind of thing. It would raise complications. So I'm
2 not inclined to do that. Of course you can raise those issues
3 at a later time.

4 You have an argument which you say is entirely
5 sufficient based on the state of the record as it existed
6 before the supplemental disclosure. LBRY is willing to have
7 these motions decided on the record as it existed before the
8 supplemental disclosure. I think that's the best way to
9 proceed. So I understand your point. I'm not willing to
10 grant all that you ask for.

11 So I will deny the motion to strike without
12 prejudice given LBRY's concession that I can decide the
13 current motions without regard to the supplemental disclosure.
14 All right?

15 So that takes care of that, which is good because I
16 want to focus on serious substantive arguments that the
17 parties are presenting here today.

18 Now, there are cross-motions for summary judgment.
19 So a question arises, who should go first, okay, and I know
20 the SEC might want to go first, but from my mind the clearer
21 way to proceed is to give LBRY a chance to go first and
22 explain why the SEC is not entitled to summary judgment and
23 while making that argument to simultaneously claim that you're
24 entitled to summary judgment, and then to give the SEC an
25 opportunity to respond to that. Because at least -- and I'll

1 ask the parties if they agree with me on this. I found quite
2 helpful the fact that LBRY did not choose a scattershot
3 approach to responding to the summary judgment motion.

4 In the SEC's opening brief they seek summary
5 judgment on the entire claim and lay out why this meets the
6 test for a security under all of its elements and notes that
7 essentially the other requirements of a failure to register
8 claim are not in dispute.

9 I think, again, LBRY has helpfully and in a focused
10 way presented a developed serious argument that this doesn't
11 meet the definition of security because of the third element
12 in the definition as refined by the First Circuit's SG
13 decision, and I would -- I assume that's the only -- I
14 understand you to make a fair notice defense argument which we
15 can engage with after we deal with the principal argument, but
16 in terms of the other elements of the SEC's case, I understand
17 you do not base either your opposition to their motion or your
18 own motion on some contention that there's a problem with the
19 other elements of a federal failure to register claim here.

20 You're attacking this on the grounds that, wait a
21 minute, under the third element of the definition of security
22 this simply doesn't meet it and therefore they can't get
23 summary judgment and in fact we're entitled to summary
24 judgment. Then I understand you to also press a fair notice
25 argument that even if we're wrong about that, there's at least

1 a triable issue on our fair notice affirmative defense.

2 So I see your argument as being quite focused and
3 developed and serious and I want to deal with those things,
4 and I don't want to deal with the other aspects of the SEC's
5 motion because I don't understand you to dispute them for
6 purposes of the current motions.

7 Is that fair? Is that a fair way to view your
8 arguments?

9 MR. MILLER: I think it is.

10 THE COURT: Okay. So we will accept that as true,
11 and I will not waste anyone's time with other issues.

12 So let's get right to it then and let's address
13 your arguments. You can speak first and explain to me why
14 this doesn't satisfy the third element of the Howey test as
15 refined in the First Circuit case.

16 And I will just -- to let the parties know about my
17 thinking, I am a judge who has a strong theory of precedent.
18 I believe I have to be a faithful lieutenant to the holdings
19 of the Supreme Court and the First Circuit Court of Appeals.
20 I find Judge Selya's decision in the SG case to be the
21 controlling precedent that I have to respect and I will --
22 unless someone convinces me that there's something about it
23 that's wrong, I'm going to follow his analytical method and
24 view both parties' arguments through the lens of what I think
25 the SG opinion teaches.

1 So just so you know, if you're going to take on SG,
2 you better do it directly and early because I'm thinking I'm
3 going to faithfully apply SG, okay?

4 All right. So that said, say whatever you want to
5 say on the issue of whether this qualifies under the
6 definition of security, and then I'll hear LBRY's response,
7 and then I'll let you say what you want to say on fair
8 notice -- the SEC's response. Then I'll hear what LBRY wants
9 to say on fair notice and hear the SEC's response to that,
10 okay?

11 With that said, I guess one other thing. Again, I
12 found your briefs quite helpful and I think I understand what
13 you're saying. You have several arguments to present, but one
14 of them that's important, as I understand it, is we're very
15 different from the other SEC enforcement actions. We're not
16 an ICO. The fact that we're not an ICO puts us in a very
17 different position from the other proceedings that the SEC has
18 commenced against others, and I'm interested in hearing what
19 you have to say about that.

20 Your principal argument, as I see it, focuses on
21 your contention that there is a consumptive use -- what I
22 think the parties call consumptive use. I might call it
23 utility use or -- but there is a use for this token and a
24 reason why people are acquiring it that has nothing to do with
25 investment potential. It has the -- it is used or consumed in

1 engaging with the LBRY app on the LBRY protocol, and because
2 of that you don't believe that it can meet the third element
3 of the Howey test.

4 I also understand you to make an argument that to
5 the extent that the value of LBC fluctuates independently of
6 any actions that the company is taking with respect to the
7 LBRY app, instead may have some correlation with the
8 cryptocurrency market generally, that that suggests that if
9 there is any expectation of profit it isn't because of the
10 actions of the developer or a third party and, therefore, we
11 don't think there's any evidence that this is principally an
12 asset that is being offered based on an expectation of profit
13 and we don't understand, even if it is, that it's an
14 expectation of profit based principally on the work of the
15 company, and for those reasons it doesn't meet the test.

16 That's what I understand your principal set of
17 arguments to be. Address them in whatever order you want and
18 add any others, but that's what I understand you to be saying.

19 MR. MILLER: Thank you, your Honor. That's very
20 helpful.

21 Before we proceed, my name is Keith Miller. With
22 me is my colleague Emily Drinkwater, my client Mr. Jeremy
23 Kauffman, and local counsel Tim McLaughlin from the Shaheen &
24 Gordon firm.

25 Thank you, your Honor, for holding this hearing. I

1 think it's an important case, a case that the crypto industry
2 is looking at very closely because it is a unique issue here.

3 This isn't SEC versus Telegram. It's not SEC
4 versus Kik where there were ICOs, where there were private
5 placement memorandums, where there were agreements whereby
6 people invested money, obtained tokens after.

7 There's something called a simple agreement for
8 future tokens. People entered into that arrangement and said
9 once the platform is built -- this is the Telegram case. Once
10 the platform is built -- we'll pay you now. Once the platform
11 is built, we'll get tokens. Now, why were they doing that?
12 Not to use those tokens, arguably. What they were doing, and
13 I think it's a fair and reasonable interpretation, was they
14 were purchasing the tokens for investment, and that's what --

15 THE COURT: So I think it is entirely relevant
16 whether something is an ICO or not, but isn't that more a
17 matter of degree rather than kind? So, for example, there's a
18 contention here, as I understand it, that at a time in which
19 there were only four videos for operation that LBRY had a
20 market cap of 1 point something billion dollars based
21 principally on its holdings of LBC, and so how is that
22 radically different from an ICO? You actually have the thing
23 up and running, but there's no real belief that anybody who's
24 acquiring LBC as of that date is doing it because of an
25 immediate plan to access one of those four videos. It's

1 because they believe that they will be a successful platform
2 in the future in the same way that an ICO purchaser would
3 believe that that application would be successful in the
4 future.

5 So it's relevant, but it's a difference in-kind
6 rather than -- a difference in degree rather than in-kind.
7 I'm seeing it that way. Is that right or wrong and why?

8 MR. MILLER: I think it's partially right, your
9 Honor, and I say I think it's partially right because what the
10 courts have said from United Housing versus Forman, a Supreme
11 Court case, to SG is the Court needs to look at the
12 promotional materials.

13 THE COURT: Right.

14 MR. MILLER: Right. And you need to look at the
15 promotional materials here. In SG, the SG case, there were
16 persistent representations --

17 THE COURT: I don't see your case as having as much
18 efforts at promoting an investment as SG. At least as
19 outlined by Judge Selya, there were very, very substantial
20 investment promotion efforts made in connection with that case
21 that seem to be more significant than the ones that occurred
22 here according to the SEC.

23 MR. MILLER: And I analogize this closer to the
24 Forman case, frankly, your Honor. In United Housing the
25 Supreme Court said --

1 THE COURT: But there are analogies -- you've got
2 to be careful with the analogy to Forman because in Forman the
3 certificates were capped. You couldn't increase the value of
4 it. And that's -- I mean, if you were Pocketful of Quarters,
5 you would be no action. And Pocketful of Quarters is like
6 Forman in that there are restrictions on the ability of the
7 token to grow in value.

8 And so I think you have to be careful of Forman. I
9 think Forman is a case where the Court was quite clear that
10 there was no investment potential there. People were buying
11 the -- I believe it was apartments, wasn't it?

12 MR. MILLER: Co-ops.

13 THE COURT: Because they wanted to buy apartments,
14 and that's different and it's more like Pocketful of Quarters.
15 I'm sure you know what that case is.

16 MR. MILLER: Yes, your Honor.

17 THE COURT: It isn't cited in the briefs, but it's
18 a no-action letter from the SEC.

19 MR. MILLER: Right.

20 THE COURT: In that case -- if you were Pocketful
21 of Quarters, we wouldn't be here.

22 MR. MILLER: Right. But I will say that under
23 Forman there's a dual purpose -- there was an argument of dual
24 purpose.

25 One purpose was people were buying these co-ops for

1 investment. They were going to flip them. They were going to
2 rent them. They were going to do certain things as an
3 investment. And the Court said let's look at the promotional,
4 let's look at the information bulletin, and that will guide
5 us.

6 And I think when you look at the promotional
7 materials, what the SEC has identified as promotional
8 materials, there aren't solicitations. They're not
9 invitations to purchase LBRY credits and you'll get a 10
10 percent profit. This isn't like SG in that regard where there
11 was a sale based on solicitation.

12 THE COURT: I think Forman -- I think the way to
13 look at this, why I think this case is interesting, I'll see
14 what the SEC says, but there is a -- there does appear to be,
15 according to the record, and I might be misreading it, a
16 consumptive use for LBC. There appears to be a consumptive
17 use for LBC. The SEC says there's a non-consumptive use.
18 Forman is a case where the Supreme Court says where there is
19 no non-consumptive use or investment use, there is no security
20 at stake.

21 Howey says where the use of it is for investment,
22 it is -- it meets that element of expectation of profit.

23 This case might be different from both Forman and
24 Howey, at least this would be I think something you're saying,
25 is what happens in a what we would call in another context a

1 mixed motive case where there is both an objective -- and let
2 me just ask this to make sure that I'm on the right track
3 here. Do you agree that the perspective that I should be
4 looking at is from the perspective of a reasonable acquirer of
5 the LBC?

6 MR. MILLER: I think that's the main test, but I do
7 also think you can look at the subjective intent.

8 THE COURT: All right. So it can play a role, but
9 ultimately in helping me see what an objective investor would
10 be -- we wouldn't call it an investor. An objective acquirer.
11 Do we agree on that?

12 MR. MILLER: Yes.

13 THE COURT: Okay. So I'm thinking that to the
14 extent this case can be helpful to people in this world that
15 your client lives in is to provide -- at least my take on what
16 you do in a case where there is a consumptive acquirer and
17 arguably some people who are not acquiring for consumptive
18 purposes, how does that fit under the third element of the
19 Howey test?

20 And I think you argue that there's a legal question
21 and a factual question.

22 I understand your brief to argue that the test
23 should be unless it is principally for investment we should
24 not treat it as satisfying the third element of the Howey
25 test. Is that the position you take at least on the law that

1 I would use?

2 MR. MILLER: Yes.

3 THE COURT: Okay.

4 MR. MILLER: I think the law is that what the Court
5 needs to look at is the principal motivation of the purchaser.
6 If the motivation --

7 THE COURT: Based on the totality of circumstances,
8 not on a characterization or label that anyone gives to it.

9 MR. MILLER: Right. The overall emphasis. What
10 was the overall emphasis. The Court uses this language.

11 THE COURT: Judge Selya doesn't use the word
12 principally in SG with respect to the first element of the --
13 first component of the third element of the SG test. He uses
14 different language. So I'm inclined to just use his language.
15 Do you think that language requires any different
16 interpretation than the principal motivation? Because what
17 you cite as far as I can see -- do you understand my point
18 that there are -- with respect to the third element of Howey
19 there are two components. One is expectation of profit and
20 the other is from the action of the --

21 MR. MILLER: Of others.

22 THE COURT: Okay. Action of others.

23 The cases you cite for the proposition using the
24 principal motivation case all deal with the second component
25 of the third element. I went back and tried to read them all,

1 and they don't -- I didn't find any case that uses that
2 language principally with respect to the first component of
3 the third element. Have I missed something?

4 MR. MILLER: I would have to -- and I apologize. I
5 believe that -- or I thought that the Forman case, and that's
6 where I was getting it from, used the word principally or
7 primarily. I know obviously the word overall emphasis has
8 been used.

9 THE COURT: Yeah, I just looked at -- I mean, I'll
10 get out Judge Selya's language. You can tell me if that's
11 wrong or not from your perspective.

12 So this issue arose -- of course you know this.
13 I'm just making it clear on the record. This issue arose
14 because Howey when talking about the efforts of others used
15 the word solely. And in every circuit that has considered
16 that after Howey said, oh, yeah, he used that word but they
17 don't really mean that word, they mean something else. And
18 Judge Selya endorses that view as well when talking about the
19 efforts of third parties or others, efforts of others, and
20 then he cites a variety of cases.

21 But when talking about expectation of profits -- so
22 he cites to Forman, you're right. "Based on its determination
23 that investors were attracted solely by the prospect of
24 acquiring a place to live and not by financial returns",
25 Forman used that for the different proposition of in a case in

1 which it is solely, because they wanted to acquire a place to
2 live, that in that case it doesn't meet the test of security.
3 And Howey uses solely in a different way, I believe, and
4 that's what courts are rejecting. But when talking about the
5 first component of the third element of the Howey test, he
6 seems to say that --

7 MR. MILLER: I believe there's one paragraph, your
8 Honor, in that section where the Court is talking about --

9 THE COURT: Yeah, I love when -- he does a great
10 job of comparing Forman and Joiner.

11 MR. MILLER: Right.

12 THE COURT: And Forman was a case in which it was
13 solely for they want to live there, not for investment. And
14 Joiner was a case where most of their value and all of their
15 lure was investment, and the leasehold interests were no more
16 than an incidental consideration to the transaction.

17 So he seems to be -- I'm inclined to take that as
18 my model when analyzing this issue. Is that right or wrong?

19 MR. MILLER: I think the first sentence of that
20 paragraph is instructive. The way in which these cases fit
21 together is instructive.

22 In Forman the apartment was the principal
23 attraction for prospective buyers. Principal. He's using the
24 idea of principal. And then he goes into Joiner and says
25 incidental. So I think those two words, principal versus

1 incidental, is what the Court needs to weigh. And that's why
2 I think the overall emphasis of the materials, the promotional
3 materials, was it principally to speculate, to have people
4 buy, to speculate, or was it principally to consume or use the
5 tokens.

6 THE COURT: Okay. I get your point. I'll be
7 interested when the SEC speaks to know do you agree that
8 that's the right way to read SG or not. You need to explain
9 why not if you think that.

10 All right. So let's set aside the question of the
11 legal test, which is not, you know, there isn't a super clear
12 statement of what the legal test is, but why factually do you
13 think in this case the SEC is wrong in contending it's
14 entitled to judgment, that the evidence construed in the light
15 most favorable to you could only cause a reasonable factfinder
16 to conclude that the expectation of profit component has been
17 satisfied here?

18 MR. MILLER: Factually there's no solicitation.

19 THE COURT: Well, there is some solicitation and
20 there is in fact some private deals for the acquisition of
21 LBC. We can't pretend those don't exist.

22 MR. MILLER: Well, there is one e-mail from one of
23 the employees to a quote-unquote prospective investor, and
24 they say you may want to buy because two or three years from
25 now it could be worth a lot of money.

1 THE COURT: But he actually sold LBC, and maybe I
2 got that wrong, I thought to a crypto club, a buying club, and
3 to this other entity. I can't remember the name of it. Your
4 client sold significant quantities of LBC to people and in
5 connection with those things certain things were said, right?

6 MR. MILLER: Right. Let me take one at a time.

7 So in connection with the club, club members were
8 buying crypto, different types of crypto, different tokens,
9 okay, and the testimony elicited from them is they wanted to
10 check out LBC and see how it could be used.

11 So there is a situation where a club -- there's no
12 evidence to suggest that the club members were specifically
13 buying it for speculation. Other ones, market makers, why
14 were they buying it? Were they buying it for investment
15 or were they buying it --

16 THE COURT: What do I glean from the fact that when
17 there were four videos available on your site you had a market
18 cap of 1.2 billion or 1 point whatever billion which was based
19 principally on the value of the company's holdings of LBC?

20 MR. MILLER: But that's an asset. It's an asset of
21 the company.

22 THE COURT: Right. But it says that the asset had
23 been bid up to a price that was extraordinarily high when
24 there was almost no current use. It wasn't an ICO, I agree
25 with you, but there was almost no current consumptive use that

1 would justify that market cap valuation.

2 MR. MILLER: Just like any other commodity -- and
3 we maintain that LBC is a commodity. Just like any other
4 commodity -- and I think we identified an analogy, I don't
5 know if it's a great analogy, but Beanie Babies, LEGOs, would
6 people argue that those are securities because the value in a
7 market -- and there's markets out there. Go on a website and
8 you can say I want to buy --

9 THE COURT: Well, if you were selling investment
10 contracts in a Beanie Baby consortium of -- we've cornered the
11 market on Beanie Babies and we're going to release them like
12 the diamond companies release diamonds and we're going to
13 control the rate at which Beanie Babies get into the market,
14 that would look like a security to me. I mean that would
15 definitely be --

16 MR. MILLER: I don't think -- well, as I said, just
17 like any other commodity. We think it's a commodity here.
18 And just because the price increased at some point in time
19 doesn't mean it's a security. It's a commodity and we will
20 argue it's a commodity because the courts have said you need
21 to look at how it's being promoted. How are you promoting it
22 and why are people interested in buying it? What's the
23 motivation?

24 THE COURT: Right. That's why I think a very high
25 market valuation for -- and I want to get terminology that to

1 your company is acceptable. I've been calling it digital
2 asset. Is that acceptable?

3 MR. MILLER: That's acceptable, yes.

4 THE COURT: All right. So when a digital asset has
5 a very, very high valuation and there is no current use for
6 it, doesn't that tell you that they are anticipating that you
7 will make the business succeed to the point that there will be
8 a substantial current use for it, and, therefore, people are
9 investing in the hope that you make the company and the app
10 much more profitable?

11 MR. MILLER: I still don't believe that that's
12 solicitation. It's not an invitation to buy. That's why I
13 think what's instructive here is these other cases the SEC has
14 brought. They involve private place memorandums. They
15 involve SAC agreements. They involve white papers.

16 THE COURT: Is there any evidence that the crypto
17 club guys wanted to use your site as opposed to -- usually
18 investment clubs make investments in a pool and in a basket of
19 things that they are trying to invest in, not that, oh, we're
20 all going to want to use LBRY.

21 Doesn't that suggest that at least with respect to
22 that purchaser that they were motivated by investment
23 potential?

24 MR. MILLER: I think there is that argument, yes.

25 THE COURT: Yeah. Okay.

1 All right. But you do make an argument, and I'm
2 interested in understanding this argument, about on-chain and
3 off-chain uses, and, you know, we're going to set aside the
4 supplemental disclosure, but help me understand a couple of
5 things about this.

6 So, first, can you give me a brief description of
7 what LBRY's business model is? How does LBRY succeed
8 businesswise?

9 MR. MILLER: Well, it's all based on users. Today
10 they have 1.5 million users visiting the site and using the
11 blockchain. 1.5 million users.

12 THE COURT: So YouTube succeeds by an advertising
13 model. You're not doing an advertising model, right?

14 MR. MILLER: They are not.

15 THE COURT: And your people who post on LBRY have a
16 great potential to reap very large rewards if they produce
17 very valuable content for which people are willing to tip or
18 pay with LBC, right? I see how those people profit.

19 How does your company profit and grow financially?
20 I understand to the extent LBC appreciates in value and you're
21 a store of LBC, the company prospers, but apart from that how
22 does it make money other than the fact it holds LBC?

23 MR. MILLER: As in a lot of startups, the purpose
24 of the startup is not necessarily to make money immediately.
25 It is to look at opportunities.

1 THE COURT: What's the business model? Eventually
2 FaceBook would make money on an advertising model. That's how
3 they started and why people wanted to invest in them. I'm
4 just trying to figure out -- and they weren't making money in
5 the beginning, you know, and I assume all of these things like
6 YouTube didn't make money in the beginning, but they had a
7 plan to make money in the long run. I just -- I needed to --
8 like, does your -- and please excuse my ignorance.

9 When someone posts something to the blockchain on
10 LBRY, on the LBRY app, right, or they basically want to have a
11 video or something, right, so there has to be an entry on the
12 blockchain for that, right? Right. Okay. And when they do
13 that, is there a transaction fee in LBC that the poster has to
14 pay?

15 MR. MILLER: So let me try to distinguish between
16 two things. One is the LBRY blockchain.

17 THE COURT: Right.

18 MR. MILLER: That's open-source software --

19 THE COURT: Okay.

20 MR. MILLER: -- that has been adopted by known
21 operators, computers, everybody that's in the system, and they
22 get a chance -- and that's where the LBRY credits are derived
23 from, from the blockchain, right?

24 THE COURT: Right.

25 MR. MILLER: You can get a credit, a LBRY credit,

1 mostly from mining, right? There is pre-mined, and then now
2 going forward somebody who validates a transaction on a
3 blockchain gets rewarded a token.

4 THE COURT: Right.

5 MR. MILLER: And that's how new tokens get minted.

6 THE COURT: Now, you said something that I need to
7 understand. I've always recognized that there's a separation
8 between the LBRY application and the LBRY -- what would you
9 call it?

10 MR. MILLER: Blockchain.

11 THE COURT: It would include the blockchain.

12 MR. MILLER: Yes.

13 THE COURT: And so I understand that the LBRY
14 blockchain is open-source like Ethereum is, for example. So
15 people can use Ethereum for whole varieties of things, and
16 you're saying they can use the LBRY blockchains for a whole
17 variety of things as well.

18 MR. MILLER: Right.

19 THE COURT: And when a block is verified, there is
20 a -- the miner earns some sort of LBC credit, right?

21 MR. MILLER: That's correct.

22 THE COURT: And the LBRY app is just one thing that
23 sits on the blockchain.

24 MR. MILLER: That's right.

25 THE COURT: Okay. And what I'm asking is, is there

1 a transaction fee that somehow your company benefits from when
2 somebody uses the blockchain?

3 MR. MILLER: Yeah. So right now I believe, and it
4 was in Mr. Kauffman's declaration, there are some 35 different
5 applications that run on the LBRY -- so each application could
6 be unique, could be different.

7 THE COURT: Right. I get that.

8 MR. MILLER: With respect to Odysee, which is the
9 LBRY-owned subsidiary that is now the application that people
10 are using, right, I do not believe there's a transaction fee.
11 That could be something in the future that is -- or it could
12 be that they decide to go down an advertising route, but with
13 most of these companies it's getting users to come to the
14 site, it's getting people to use the business, and that's the
15 first step.

16 THE COURT: I understand you want to build a user
17 base, but there needs to be a business model. I'm just trying
18 to understand what it is.

19 I understand part of the model is if we hold a
20 gigantic amount of LBC, that's going to become way more
21 valuable and we're going to be all wealthy because of it, and
22 people who own shares of our company are going to be
23 multimillionaires. That's great.

24 Apart from that, what's the business model?

25 MR. MILLER: I don't think they've figured out how

1 to definitively monetize that at this point in time.

2 THE COURT: Is it fair to say as it currently
3 stands the business case for making money that we identify is
4 growing the value of LBC?

5 MR. MILLER: I don't think that's a fair
6 interpretation.

7 THE COURT: Then what is it?

8 MR. MILLER: I think it's growing the network of
9 users.

10 THE COURT: Right. Growing the network of users
11 might be a very good public benefit, but you've got to make
12 money, and I'm just asking how do you make money. If you are
13 pitching me -- think I'm the venture capitalist who wants to
14 give you a couple million bucks. Tell me how I'm going to
15 make money within the next ten years. Answer the question for
16 me. Tell me. I'm your venture capitalist.

17 MR. MILLER: There are different ways to monetize
18 it. One's advertising, which is like YouTube. YouTube is all
19 advertising fees.

20 THE COURT: But you distinguish yourself from
21 YouTube in that you're not an advertising model, and you don't
22 have an algorithm that you need if you're going to have an
23 advertising model, and you have nonintrusive limited content
24 moderation, and those are things that distinguish you from
25 YouTube. To the extent you want to just be YouTube on a

1 blockchain, that is not what I understand you to be aspiring
2 to.

3 MR. MILLER: No, not necessarily, but that doesn't
4 mean they can't change if they need to get monetized, right?
5 Another way is transaction fees, like you said. I do not
6 believe neither of those things are --

7 THE COURT: But there's nothing going to them now?

8 MR. MILLER: Right, but -- yes, it's an asset.
9 LBRY credits are an asset. So you can't ignore that. A
10 venture capital company coming in would certainly look at that
11 and say how many credits do you have and what's the market
12 value of it. Certainly.

13 THE COURT: Could your company choose to run its
14 business like Pocketful of Quarters and use a digital asset
15 that has limitations on its ability to grow in value which
16 could still be used at a designated fixed rate to compensate
17 miners and to perform other functions but that would not have
18 any -- it would be like Forman, not having any investment
19 potential?

20 MR. MILLER: It could. It could, but I would go
21 back to why was this developed. This was developed as an
22 alternative to other -- it's to allow publishers --

23 THE COURT: I fully get how -- you know, just
24 saying LBRY is YouTube on a blockchain says a lot because a
25 blockchain operates very differently from a company like

1 YouTube. So we don't want to diminish that. I agree it's a
2 very different kind of enterprise. I'm just trying to figure
3 out -- the concern I have is to the extent that LBRY is -- its
4 business model is grow the value of LBC, and you grow the
5 value of LBC by building uses on the blockchain that make LBC
6 more valuable to users, other people who acquire LBC not for
7 they want to use it on LBC but they are bolstered in their
8 desire to buy LBC as an investment because, like the company,
9 they think LBC is going to grow in value because LBC is going
10 to do stuff to help it grow in value and LBC is incentivized
11 to do stuff to help it grow in value.

12 That's my concern and that looks a lot like
13 expectation of profit.

14 MR. MILLER: Well, but I think what Forman and SG
15 say is you need to look at the promotional material, not
16 ultimately how could --

17 THE COURT: Not just the promotional material, but
18 you do look at the promotional material. I agree.

19 MR. MILLER: Right. That's where I think we have a
20 difference of opinion with the SEC. There is no solicitation.
21 I think -- you know, Section 5 is the offer or sale, and
22 typically in all the cases, including, you know, SG, even SEC
23 versus Smith which SEC cites in their brief, there are offers.
24 Somebody offers, says this is a great deal, you're going to
25 make 10 percent.

1 The language -- when you look at the language here
2 that they've identified --

3 THE COURT: And you've pointed out there are
4 disclaimers, you know, don't buy it for -- you know, we have a
5 one billion plus valuation, but that doesn't matter.

6 MR. MILLER: Focus on the -- ultimately, focus on
7 this network.

8 THE COURT: There are a number of those kinds of
9 statements in the record. As well, I have to take issue with
10 you because -- and LBRY -- excuse me, SEC when it has its
11 turn -- its brief does identify a number of things that they
12 think are solicitation materials that touts the investment
13 value of it. So, I mean, we shouldn't pretend that the SEC
14 doesn't cite anything. What they cite you say may be
15 insufficient when you look at it considering the total mix of
16 available information about LBC that the company is putting
17 out, but they did make -- your company did make sales of LBC
18 and they did make statements about the growth in value of the
19 LBC asset. Maybe that's not enough, but it is there.

20 MR. MILLER: I don't think it's enough, and I think
21 I would direct the Court to Rice versus Branigar. It is an
22 Eleventh Circuit case, but in that case the Court said passing
23 references or mere mentions of the possibility that an item
24 could increase in value do not necessarily transform a
25 transaction into an investment company.

1 THE COURT: I agree with that.

2 MR. MILLER: And that's our point here. If you
3 look at what these statements are, LBRY is not out there
4 saying, hey, everyone, buy LBRY credit. That's not -- you
5 need to take the overall emphasis of the promotional material.
6 And what's principally or significantly here, not incidental,
7 what's principally and significantly being mentioned? And
8 it's not focused on buy LBRY you're going to make money. It's
9 use the network. Because just like Naomi -- the declarants,
10 we had five declarants along with 300 others. Brockwell.
11 That's it. Naomi Brockwell. Just like she said, I've made a
12 business out of this. And the same thing with the other four
13 declarants. I've made a business out of this. On YouTube I
14 wasn't getting any advertising money. Why? Because I didn't
15 have enough views. I've gone to LBRY and now I'm getting
16 tipped. I'm getting people purchasing. And that's what LBRY
17 wanted to accomplish.

18 THE COURT: I think this record does contain
19 evidence that there are consumptive uses for LBC. I think
20 that's undeniable, you know, and it's a question of looking at
21 the total mix of available information, looking at the
22 economic reality of the situation, and trying to consider no
23 one piece of evidence as dispositive here and looking at it to
24 see whether the standard for summary judgment is met.

25 Can I ask you about -- again, this is an

1 opportunity for me to kind of clarify gaps in my knowledge
2 here. When we talk -- both of you talk about on-chain and
3 off-chain uses and you seem to talk as if something is an
4 on-chain transaction, that that is necessarily a consumptive
5 transaction, and I don't understand that to be the case. I
6 understand you can definitely have off-chain transactions
7 which are not likely to be consumptive transactions, and I
8 understand you have on-chain transactions, but I don't know
9 why you can't have on-chain transactions which are both just
10 as much investment transactions.

11 If I want to buy the LBC in your wallet and instead
12 of having an off-chain side contract I believe in blockchain
13 and I want to have that asset in my wallet, we would do an
14 on-chain transaction for me to make my investment. So I don't
15 know that the proxy that the two of you are using between
16 on-chain and off-chain really is as perfect as you seem to
17 suggest it is.

18 Now, maybe that's a misunderstanding on my part.
19 Is it a misunderstanding on my part?

20 MR. MILLER: No, your Honor. On-chain transactions
21 can include transactions for consumption and it can include
22 transactions that an exchange, for example, has put on it.

23 THE COURT: Am I safe in assuming, because
24 otherwise the SEC would have produced it, that your company
25 has no way of identifying precisely which LBC transactions are

1 consumptive and which ones are not?

2 MR. MILLER: The only way you would be able to do
3 that is to have the wallet addresses of all the exchanges and
4 to be able -- so when someone does a transaction on exchange,
5 for the most part they don't automatically hit the blockchain.
6 Why? Because they have an internal ledger. It's internal.
7 They have LBRY credits. One person wants to buy. One wants
8 to --

9 THE COURT: You say internal to the two of them?

10 MR. MILLER: No. Internal to the exchange. The
11 exchange says I've got a thousand LBRY credits. Someone wants
12 to buy ten of them. Okay. I'll take --

13 THE COURT: When you say the word exchange, what
14 are you referring to?

15 MR. MILLER: An asset exchange.

16 THE COURT: Oh. Coinbase or something?

17 MR. MILLER: Coinbase. Exactly.

18 THE COURT: So you're saying that Coinbase has a
19 giant wallet of LBC and it's just assigning certain LBC in its
20 giant wallet from this person to that person?

21 MR. MILLER: Right. In their ledger.

22 THE COURT: Yeah.

23 MR. MILLER: But there are obviously times where it
24 may be a big purchase, right, where they have to come and --

25 THE COURT: If you buy LBC at Coinbase, right,

1 you're telling me, and I think that's what I've understood,
2 there isn't an entry on the LBRY blockchain of Barbadoro has
3 just bought four LBC.

4 MR. MILLER: That's right.

5 THE COURT: And there's no entry on the blockchain
6 except ultimately the wallet that Coinbase has on the chain
7 has a number of LBC in it, and then Coinbase either with an
8 internal ledger or a contract between the parties or something
9 engages in an off-chain transaction, right?

10 MR. MILLER: That's correct.

11 THE COURT: Okay. And if I want to use my LBC to
12 tip somebody, don't I need it in my wallet?

13 MR. MILLER: Yes.

14 THE COURT: In my LBRY wallet?

15 MR. MILLER: Right.

16 THE COURT: Okay. So tipping would necessarily be
17 an on-chain transaction.

18 MR. MILLER: That's correct.

19 THE COURT: Paying somebody, at least if I'm using
20 the blockchain -- I could go to a side transaction, I suppose,
21 and say, oh, you know, my law clerk is posting something on
22 LBC and I really want to view the private part of it, I want
23 to pay his ten LBC credits, I can call him up on the phone and
24 say, look, can I just send you a check and will you let me in,
25 and they probably could, couldn't they?

1 MR. MILLER: Sure.

2 THE COURT: It's possible to have an off-chain,
3 but, generally speaking, I would assume that to the extent
4 things are on-chain -- that if you want to do a consumptive
5 use, the ordinary use would be an on-chain use, right?

6 MR. MILLER: That's correct.

7 THE COURT: Okay. And off-chain uses are not
8 directly ordinarily tied to consumptive uses. Do you agree
9 with that?

10 MR. MILLER: Well, except for in the
11 situation which if you wanted to, you have to --

12 THE COURT: But that's not the way it's designed to
13 work. I mean, if you're a blockchain person, you don't want
14 to be running your life with individual private ledgers with
15 people. You believe in blockchain.

16 MR. MILLER: Yes.

17 THE COURT: And blockchain is a public ledger, this
18 one is, and this public ledger is what you would use for your
19 on-chain transaction in the ordinary course.

20 MR. MILLER: That's correct.

21 THE COURT: Fair to say?

22 MR. MILLER: Yes.

23 THE COURT: So it's not a complete, perfect
24 substitute but is a rough indicator perhaps of the ratio of
25 on-chain to off-chain uses? Does that make sense?

1 MR. MILLER: I think it's fair, yes.

2 THE COURT: All right. Good.

3 Sorry to interrupt. Say anything else you want to
4 say. This has been very helpful in educating me.

5 MR. MILLER: We also think -- besides the objective
6 analysis of what a reasonable investor would believe, we also
7 believe that some of the case law allows subjective, and for
8 that reason we would argue that the 300 or so declarations --
9 and those declarations, what did they say? Look at them.
10 They said I purchased on exchanges not as an investment. For
11 use. I needed LBRY credits. Where do you get LBRY credits?
12 Well, you can mine them or you can buy them. So that's
13 important. That's important.

14 So the theory of, gee, people are buying them on
15 exchanges and therefore they're speculators --

16 THE COURT: You can't -- I've never looked at the
17 LBRY app because I believe I need to make my decision based on
18 what you people tell me.

19 MR. MILLER: Right.

20 THE COURT: But I don't think you can tip somebody
21 off-chain, can you?

22 MR. MILLER: No, you have to -- the point here is
23 when you buy --

24 THE COURT: Am I right, though? To tip you've got
25 to be on-chain?

1 MR. MILLER: Yes.

2 THE COURT: To buy on the app itself, to buy
3 access, you've got to be on-chain.

4 So you buy your Coinbase LBC. Unless you instruct
5 Coinbase I want an on-chain transaction from your wallet --
6 the off-chain transactions can't be used to tip or to buy
7 unless you've tried to do kind of a workaround, an off-chain
8 workaround, which isn't the way the app is designed to work,
9 right?

10 MR. MILLER: Right. Your LBRY wallet is where you
11 tip from, okay, where you purchase from.

12 THE COURT: Right. So if you buy your LBRY at
13 Coinbase and there's an internal transfer in the Coinbase
14 ledger, you can't use that LBC to tip.

15 MR. MILLER: Unless you transfer to your LBRY
16 wallet.

17 THE COURT: Right. And then it's an on-chain
18 transaction.

19 MR. MILLER: Right.

20 THE COURT: Okay.

21 MR. MILLER: So the point here is the SEC argues
22 that there's all this exchange activity, right, and therefore
23 that's speculative. People are buying -- and I think it's a
24 faulty premise. People are buying on these exchanges,
25 Coinbase, all the exchanges, for speculation, and our

1 declarations prove the opposite. That's not true. There's no
2 evidence that the SEC has presented to show that people were
3 buying on exchanges for speculation.

4 Now, is it logical? Yes. But there's no evidence
5 in the record that says -- we don't have one affidavit from an
6 investor to say --

7 THE COURT: I haven't scrutinized these affidavits
8 yet. Do your LBC uses for business people, do they say that I
9 acquire LBC in an off-chain transaction, or do they say I buy
10 on Coinbase and tell them I need the actual LBRY in my wallet
11 because otherwise I can't use my, you know, I can't use my
12 LBRY?

13 MR. MILLER: They don't go into that type of
14 detail, but they say I bought on an exchange and then
15 subsequently have used it on LBRY to tip, to stake.

16 THE COURT: But we've just agreed mechanically,
17 except in an extraordinarily unusual circumstance, it would
18 have to involve an on-chain transaction to do that.

19 MR. MILLER: Right.

20 THE COURT: Okay.

21 MR. MILLER: I will correct one thing that my
22 client has told me, and that is the Odysee entity, subsidiary,
23 the new entity that is the app that is running makes money
24 through advertising and credit card processing. So there is
25 money being generated by Odysee through advertising --

1 THE COURT: Okay.

2 MR. MILLER: -- and through credit card processing.

3 THE COURT: But the LBRY app doesn't do
4 advertising, right? I thought one of the things you
5 differentiate yourself from YouTube is you don't do
6 advertising.

7 MR. MILLER: We didn't, but now the -- and that was
8 when LBRY.com or LBRY TV, okay, at that point in time during
9 the generation as it expanded, it did not. I'm being told now
10 that the new entity Odysee that is the app that everyone is
11 using is charging a processing fee for credit cards, okay, and
12 is doing advertising.

13 THE COURT: Okay. All right. That's helpful.

14 MR. MILLER: So I just wanted to clarify that.

15 THE COURT: Okay. Good. I appreciate that.

16 How about the -- unless you have something more to
17 say about the first component, you also have an argument on
18 the second component, based on the effort of others, and your
19 argument -- it's one that I haven't seen in the case law
20 anywhere else, but your argument is LBC fluctuates in value
21 for reasons unrelated to LBRY's activities in building the
22 site. If we did a -- oh, like if you had to do a loss
23 causation argument in an SEC fraud case like I've had to do in
24 several cases, you would have to separate out market
25 fluctuations from movements in the individual stock for

1 reasons that aren't ordinary market fluctuations.

2 It's very common for all kinds of investments to
3 tend to move as groups, and I think what the SEC is saying to
4 you is that doesn't mean a thing. That doesn't in any way
5 support your argument. It still is bought for investment
6 because they want it to go up for reasons other than the labor
7 of the person that has the LBC. And when they talk about
8 efforts of others, in order for LBC to be viable as a currency
9 the LBRY blockchain has to continue to function and LBRY has
10 to make that LBRY blockchain continue to function. And,
11 therefore, it's the efforts of LBRY that allow for
12 cryptocurrency movements of LBC to be coordinated with Bitcoin
13 and Ethereum and a bunch of others, and that doesn't in any
14 way undermine their claim that this is being marketed and sold
15 for the investment potential based on the work of others.

16 That's what I understand the SEC to be saying to
17 you why your argument fails. What's your response?

18 MR. MILLER: So efforts of others. The efforts of
19 others in a blockchain is all the note operators. Everyone
20 has a say. Everyone can do things.

21 And we said -- in Mr. Kauffman's declaration he
22 identifies how many times --

23 THE COURT: Is the LBRY blockchain like the Bitcoin
24 blockchain? There's nobody running the Bitcoin blockchain.

25 MR. MILLER: Exactly. And just like Ethereum.

1 THE COURT: And you're saying there's no one
2 running the LBRY blockchain?

3 MR. MILLER: That's right. Now, certainly --

4 THE COURT: Your client doesn't do anything except
5 promote it?

6 MR. MILLER: No. No, I wouldn't say that. They
7 certainly do do things on the blockchain. Tweak it, right?
8 They talk to other members, the LBRY Foundation.

9 THE COURT: I mean, they could go out of business
10 today and the LBRY blockchain would continue in perpetuity
11 just like the Bitcoin blockchain.

12 MR. MILLER: Absolutely. And anyone could offer
13 some software code adjustments. And if it's adopted by all
14 the members, it takes off.

15 THE COURT: Okay. All right. So that's your --
16 that would be your point. LBC's viability only depends on the
17 LBRY blockchain continuing to function. To the extent it
18 fluctuates in price, it's based on speculation because of
19 people who are speculating based on cryptocurrency values,
20 cryptocurrency as a sector of a market, say for example, and
21 that isn't efforts of others as meant by Howey.

22 MR. MILLER: That's correct. That's correct.

23 THE COURT: Okay. Anything else you want to say
24 about that?

25 MR. MILLER: Just, again, there are approximately

1 35 applications that are running on top of -- if Odysee
2 decides to go poof, it doesn't matter. Those other
3 applications are still going to be running on the LBRY
4 blockchain, and LBRY, Inc. has no control over that.

5 THE COURT: Okay. Good. Thank you.

6 MR. MILLER: Thank you.

7 THE COURT: Let me hear from the SEC and your
8 response to what you've heard.

9 MR. JONES: Thank you, your Honor. Give me a
10 moment to carry all my stuff over here.

11 Your Honor, just for the record, Marc Jones for the
12 Securities and Exchange Commission.

13 If I can pick it up right there where we left off
14 on efforts of others.

15 THE COURT: All right.

16 MR. JONES: LBRY did not run an ICO but instead
17 allocated credits for various purposes. The only way those
18 credits are worth something in the future is if LBRY delivers
19 on their promises to create a revolutionary way to share and
20 monetize content. That's Exhibit 49, Plaintiff's Exhibit 49.

21 It's not credible and it's not true that there is
22 no expectation of profits based on the efforts of LBRY. LBRY
23 told people again and again that LBRY credits would go up when
24 they developed the network and that they were spending tens of
25 thousands of hours to develop that network.

1 Now, that's the factual point there. The efforts
2 of others are absolutely -- LBRY said again and again, we are
3 developing this network. We are solely focused on it. We are
4 in it for the long term. Don't look at the short-term price
5 of LBC because in the long term it's going to go up. In the
6 long term, as we develop this network, us.

7 In fact, they said you don't get a very good
8 product -- you don't get a very good software product when you
9 leave it to the masses. You have to have somebody focused on
10 doing it.

11 THE COURT: Well, it is open-source. People can
12 contribute to its development.

13 MR. JONES: Absolutely, your Honor, and legally
14 that's fine. It doesn't actually have to be the efforts of
15 LBRY solely. It has to be the efforts of someone other than
16 the purchaser.

17 That's the point in the Howey test. If you buy
18 something and you're gonna -- you know, if you buy a
19 fixer-upper house and you're gonna fix it up and make it worth
20 more, that's not the efforts of others.

21 If you buy something from LBRY because you think
22 Odysee, their wholly owned subsidiary, is going to make it go
23 up in value, that's okay.

24 THE COURT: I mean, I think the principal concern
25 underlying the efforts of others requirement is to deal with

1 situations in which the person acquiring the asset is also
2 involved in some significant way in the decision-making and
3 functioning of the business.

4 MR. JONES: As a partner.

5 THE COURT: That would be the clearest example.

6 MR. JONES: Right.

7 THE COURT: But say, for example, you had a LLC
8 where someone was a non-working member, just an investor
9 member or something like that. Then you would have questions.
10 If they don't have any voting rights in the company, if they
11 don't have any decision-making responsibility, then they are
12 purely an investor and whatever money they make on it comes
13 from the return on their capital invested in the business.
14 That's an example of where you have a business with a bunch of
15 people undertaking effort in someone who's not -- who is a
16 member of the organization, they've contributed capital, but
17 they've signed away their vote and they have agreed not to be
18 involved in the business in any way. Sales of those kinds of
19 interests would be investment contracts I would suspect.

20 MR. JONES: They can be, your Honor, yes.

21 And on this point, on the point that your Honor was
22 making about the price of LBC can fluctuate based on the
23 overall market or competitors in the market just like any
24 other security, and in fact it is defendant's expert who puts
25 the falsity to the way that Mr. Miller was putting it because

1 defendant's expert actually says, well, when LBRY makes an
2 announcement about its team or about an idea or puts out a
3 general blog post, no price change. And we take some issues
4 with that event study and the soundness of it. You got 20
5 pages from us on that earlier this week, unfortunately.

6 But what the expert from LBRY, Exhibit 2, says is,
7 "When LBRY announces new functionality, you do see some
8 statistically significant price changes," which you would
9 expect because LBRY has told everyone, as I just quoted to the
10 Court, that when we develop this network, as we develop it, as
11 it becomes more useful, as it becomes more desirable for
12 users, LBC is going to go up. Expect the profit from our
13 efforts.

14 THE COURT: So let me ask you though -- let me
15 pursue the opposite extreme case. So I understand you're
16 saying, well, there's plenty of evidence here to suggest that
17 there's an expectation of profit because of LBRY, but what if
18 they're trying to just ride a tulip bulb frenzy case and they
19 say the way you get into this crypto market is you create a
20 new digital asset and people are buying it up without any
21 prospect of its future performance just because they are --
22 and you get into it and try to sell it on the grounds that,
23 look, we're not going to do anything to develop this product,
24 but once we issue this coin, you can buy it, and like all
25 crypto coins they're going to go up in value tremendously.

1 That would be okay with you? That would not be a
2 security if you were trying to sell your coin under that
3 theory? We won't do anything, but the market will take care
4 of it. Because I think there are a lot of skeptical people
5 about cryptocurrency that suggest that's really why it goes up
6 in value, not because of any good work or bad work that any
7 company does.

8 MR. JONES: Your Honor, absolutely there are
9 certainly lots of cases of fraudulent coins out there but --

10 THE COURT: I'm not even saying fraudulent. Just
11 direct upfront. We're not doing anything to increase the
12 intrinsic value of this coin. The market will take care of
13 it. You decide. But look at what's happened to all these
14 other coins. And you get in and you buy a few thousand
15 dollars of it, and you know a bunch of other people are going
16 to jump on it and buy a few thousand, and it's going to go up
17 as long as I can dump it quickly. The company hasn't engaged
18 in any fraud. They said right upfront what they're doing.
19 Would that not be a security?

20 MR. JONES: Your Honor, I may have to think about
21 that. I've never seen an instance solely like that.

22 THE COURT: Yeah. Well, I mean they -- the crypto
23 people themselves don't believe that the whole thing is a
24 tulip bulb frenzy.

25 MR. JONES: No, your Honor. Certainly. And

1 certainly even things that have been created as, you know,
2 joke coins have become valuable I think largely through the
3 promotions of the people who create them in the first place
4 and the people who hold a lot of them, and that's the
5 situation we have here. It's not a joke coin. It does have
6 some utility, but they created it. They created an intangible
7 item called an LBC. They did it for the express purpose of
8 funding the building of their business. They told everyone
9 that's what they're doing. That's what they did.

10 They held onto 400 million of them. They've gotten
11 rid of about half of that now, but they still have a
12 substantial amount. They told everybody, and particularly
13 people who wanted to invest in the business, we think when we
14 become the platform of choice this will be worth a billion
15 dollars or more. You should get in with us.

16 THE COURT: You cited your strongest piece of
17 evidence about why this is based on -- expectation of profits
18 based on the activities of LBRY. Is there any other evidence
19 you want to point out on that particular component of the test
20 other than what you've just referred to?

21 MR. JONES: On the efforts of, your Honor?

22 THE COURT: Efforts of others.

23 MR. JONES: I think on page 8 of our original
24 brief, and then again in the original reply, we've cited a
25 bunch of different statements by LBRY. You know, the token

1 has value in proportion to the usage --

2 THE COURT: And most of those are expectation of
3 profit but not specifically due to the activities of LBRY, and
4 I want to get to those because that's important.

5 MR. JONES: Yes, your Honor. Sure.

6 We've actually made two lists in the brief. The
7 list here on page 8 is actually LBRY talking about its own
8 efforts.

9 So, for instance, here in Exhibit 52 LBRY says,
10 "LBC will go up when we've (LBRY) built a product that is
11 compelling enough to change people's habits. We'll be
12 focusing all our efforts entirely on creating a product that
13 people will love."

14 There are several of those statements. They're all
15 in the brief. I don't need to read them all.

16 THE COURT: Okay. I just want to be sure we review
17 them carefully when we evaluate your argument.

18 MR. JONES: Yes, your Honor.

19 And the way that it is -- and there are two prongs
20 of the third prong test, but they do overlap.

21 The way that LBRY has set up this whole system,
22 there is expectation of profits from LBRY's efforts. Just --
23 and I'll sort of shade into the first part of the prong.

24 THE COURT: Do you concede that there is what I
25 think LBRY is calling a consumptive use for LBC?

1 MR. JONES: We do, your Honor.

2 THE COURT: Okay.

3 MR. JONES: Not for the entire time of the
4 offering. The offering starts in 2015. People are promised
5 LBC for services. People are paid in LBC or executives make
6 agreements that, you know, their companies that are providing
7 efforts to LBRY are going to get LBCs later, but through most
8 of it --

9 THE COURT: When would you say is the first
10 offering to the public of LBC?

11 MR. JONES: Well, so in July -- I think it's the
12 end of June of 2016 the LBRY blockchain goes live. On July 4,
13 2016, LBRY makes an announcement. It's a symbolic day.
14 Freedom at last. LBC is available for you to get. It's being
15 mined. You can get it. In 2017 and 2018 the LBRY starts
16 selling on those digital asset platforms, the exchanges.

17 THE COURT: At one point it was selling on its own
18 on the LBRY app, wasn't it? Couldn't you buy --

19 MR. JONES: Yes, your Honor. LBRY did in fact
20 engage a third party service provider called MoonPay in 2020
21 and 2021 to allow people to come with their credit cards or
22 Bitcoin or whatever and get on the app LBC. That was very
23 late in the game, not so long before this case was filed, but
24 there were eventually abilities to buy on the app. But from
25 2015 on LBRY was in one way or another continuously offering

1 LBRY through user reward programs, through employee
2 compensation, through employee purchase programs, through
3 digital platform sales, through its --

4 THE COURT: When does something that has a
5 consumptive use and that LBRY would say is a commodity shade
6 over into a security?

7 MR. JONES: Well, your Honor, I first would say you
8 don't start with the presumption that something is a
9 commodity. You apply the Howey test in the first instance.

10 THE COURT: Right.

11 MR. JONES: You should look at it. And in this
12 case from the first instance with LBC there are promises made
13 and a reasonable expectation on the part of a purchaser that
14 they can buy this thing. In fact, there were what we see in
15 these cases a fair amount, you know, get in early while the
16 price is low when we're building this thing and it's going to
17 go up. There were representations made that there were going
18 to be profits and that LBRY was going to -- there was going to
19 be a rise in value of LBC. I don't want to say the word
20 profit was used, but there would be a rise in value in LBC
21 based on LBRY building this network that it was building, and
22 in fact those representations were made before even the
23 blockchain and therefore the LBRY service went live.

24 THE COURT: What's your take -- so I think LBRY's
25 counsel did a good job of drawing my attention to Judge

1 Selya's discussion of Forman and Joiner, and they cite in
2 their brief cases that deal with their expectation of other
3 cases, but they talk about you don't have to prove it solely
4 for investment purposes.

5 So if you don't have to prove it solely, what is
6 the test, and what does the SEC say is the test for
7 expectation of profit? It's not solely. You would I'm sure
8 agree it's not solely because Judge Selya says it's not
9 solely.

10 Do you agree that it's principally? Do you agree
11 that -- do you have a view that there's some other test? What
12 is it that you say is the legal refinement of Howey and Joiner
13 and Forman?

14 MR. JONES: Your Honor, I think I would start by
15 saying that the test does not turn on the intent of the
16 purchaser alone. All of the cases that deal with Howey talk
17 about looking at the economic realities of the transaction.

18 THE COURT: I agree with that. So we don't use
19 labels. We don't use any one factor. We focus on the
20 economic realities. But we're asking, I thought given the
21 economic realities, would a reasonable acquirer of this be
22 acquiring it principally, not incidentally, whatever your
23 test, as an investment. And that would be -- you would view
24 it from the eyes of a reasonable acquirer given the total mix
25 of information and the economic realities of what is going on.

1 But then you still have to ask in a mixed motive case if some
2 acquirers are acquiring for purely consumptive and others are
3 acquiring purely for investment, what is the test by which a
4 judge evaluates that kind of a case, which I don't think any
5 of the cases I've seen have really evaluated in detail those
6 kinds of -- that kind of problem, and that's what we seem to
7 have here.

8 I think it's undeniable that people are acquiring
9 LBC for investment reasons. I think it's undeniable that
10 people are acquiring LBC for consumptive reasons. How do I
11 determine in a case like that whether something is acquired --
12 a reasonable investor considering the total mix and not
13 looking at any one factor determine -- where some investors
14 are acquiring for consumptive and some investors are acquiring
15 for investment, how do I determine whether in that case it
16 meets the first component of the third element of the Howey
17 test?

18 MR. JONES: Your Honor, I agree it is a tricky
19 problem not fully addressed by the law. And, in fact, there's
20 a third possibility, which is what if someone buys a thousand
21 LBC wanting to spend 10 and hold onto 990.

22 But I think part of the way to solve this
23 conundrum, your Honor, is to take a step back and to realize
24 that neither utility nor subjective intent --

25 THE COURT: They're not dispositive. Are you

1 saying they're irrelevant?

2 MR. JONES: I'm not saying they're irrelevant.

3 THE COURT: Okay.

4 MR. JONES: I'm saying they're not -- that they do
5 not --

6 THE COURT: They're not dispositive. They're not
7 irrelevant.

8 See, judges -- you know, maybe it's a fault.
9 Judges like to have standards against which to analyze things.
10 Otherwise, it looks like we're just making it up as we go
11 along.

12 I'm trying to have you help me --

13 MR. JONES: Yes, your Honor.

14 THE COURT: -- formulate the correct standard in
15 what you might call a mixed case where investors are acquiring
16 -- or people are acquiring the digital asset some for
17 consumptive reasons, some for investment reasons, some mixed
18 investment and consumptive reasons. At what point does the
19 expectation of profits test justify a conclusion that that
20 component of the test is satisfied? What formulation? What
21 language do you think I ought to use to describe that
22 component of the test?

23 MR. JONES: Your Honor, let me put where I think it
24 comes out, and then let me take a step back and try to justify
25 that.

1 THE COURT: All right.

2 MR. JONES: I think it comes out can a reasonable
3 purchaser expect to profit. It's not do they. It's can they.

4 THE COURT: I agree it's not do they. I agree it's
5 can.

6 MR. JONES: Can.

7 THE COURT: But if a reasonable acquirer -- let's
8 say it came out that 70 percent of the people that bought
9 LBC -- we actually dragged every LBC purchaser into court, put
10 them under oath, asked them, why did you buy it, what's your
11 evidence, or we had definitive -- apparently there is no
12 evidence that definitively shows which are consumptive uses,
13 but if we had all of that and we could nail down absolutely
14 and the conclusion I came to at the end is 75 percent of LBCs
15 were used and bought for consumptive purposes, people realized
16 that there are also promotion of this for investment, and 25
17 percent were buying because of investment, would that make it
18 expectation of profits?

19 MR. JONES: Your Honor, I want to suggest to the
20 Court that that would be a tough test to both implement and --

21 THE COURT: What if we flipped it and it was 25
22 percent wanted to use it for consumptive uses and 75 percent
23 didn't? Would that be a -- they wanted to use it for
24 investment first. Would that be a security, meet the
25 component of that test?

1 MR. JONES: Your Honor, I think in neither case
2 does the ratio actually help the Court or a securities issuer
3 to determine whether it is a security or not. That is why the
4 economic reality -- and it's not just labels have to be issued
5 and all that. Part of the economic realities test is what's
6 really going on with this thing. When you buy it, when it is
7 a transaction in commerce, what's happening?

8 What's happening here is you can buy this thing.
9 You can wait. LBRY can continue to develop its network and it
10 will be more. According to them and according to some other
11 evidence that I'm sure you want me to get to, it will go up.
12 And, therefore, whether or not I want to take part of it and
13 spend it on my cat videos, it's still an expectation of
14 profits if I am a reasonable purchaser.

15 Now, let me take a step back and try to justify
16 that in the case law a little bit.

17 THE COURT: I don't want anybody to think I'm
18 confused about this. I don't think subjective intentions is
19 the determining factor here.

20 MR. JONES: No, our Honor.

21 THE COURT: I just don't read the cases to say
22 that, but I don't think the cases provide a good answer right
23 now, a clear-cut line drawing kind of answer between -- that
24 you use to address cases in which there is a viable
25 consumptive use. I mean, SG -- there might be a consumptive

1 use in SG as well if you think about it. They don't really
2 discuss that in -- this case doesn't discuss it in detail. It
3 focuses primarily on things like how is it promoted, how was
4 it -- in connection with where it was sold, what was going on,
5 and the economic reality of that situation looked at in a kind
6 of holistic, practical way, is it being sold in such a way
7 that people are -- a reasonable investor given the total mix
8 of available information and the economic realities of really
9 what is going on buying that non-incidentally for investment
10 purposes.

11 I think that seems to be the way I would take the
12 test, and maybe it doesn't matter whether you use the word
13 principally or not incidentally, but that's the kind of thing
14 of which Supreme Court decisions are made, and I don't like to
15 make decisions that are going to be resolved by the Supreme
16 Court. I like to decide things so that at my level that's the
17 end of it. People just agree that it's right. So it may not
18 matter, but I am just giving you your chance now to tell me if
19 you think there's a -- LBRY has suggested the language for the
20 legal test. You haven't. So if you've got any language,
21 now's your time.

22 MR. JONES: Your Honor, I would go to what I just
23 said. Can a reasonable purchaser expect profits as opposed to
24 what is the reasonable purchaser's intent. What is 65 percent
25 versus 35 percent? Can they expect profit?

1 THE COURT: You don't have a case that says that.

2 MR. JONES: So this is interesting, your Honor.

3 This is where I want to talk about SG and Forman.

4 In SG -- let's start with Forman.

5 The Court actually goes through, okay, you can't
6 sell this thing for a profit, you're prohibited, but let's go
7 through -- you know, clever plaintiffs with a financial
8 interest came up with a few possible profits, and the Court
9 actually exhausts each one of those and says, no, that is not
10 expectation of profits, that is not expectation of profits,
11 that is not expectation of profits, those are profits, and it
12 exhausts the whole thing. And that suggests that the Court at
13 least in Forman and in the subsequent cases where they're
14 looking at mostly housing, some of these EB-5 visa cases, but
15 mostly housing, is there anything there beyond you just want
16 to consume it. And if there is, then maybe the Court was
17 wrong to dismiss or wrong to give summary judgment, but is
18 there anything there.

19 And here SG confronts this question squarely in my
20 opinion, your Honor, because the principal defense in SG was
21 this is a game. This thing you're buying from us, you're
22 playing a game. And, yeah, you may make some money from it,
23 but you're playing. You're getting the utility of the game.

24 And Judge Selya says that doesn't matter. In fact,
25 that's how the lower court had decided and said it's a game.

1 It's not a transaction in commerce. It doesn't look like a
2 securities transaction. And Judge Selya comes along and says,
3 no, what's actually going on here, there actually is a profit
4 motive here. Although he doesn't deny that there's a game
5 aspect to it and that some people may be playing because
6 there's a game. He simply looks at it and says it doesn't
7 matter that it's a game. It doesn't matter that there's a
8 utility. Because there was a utility in the oranges and the
9 whisky casks and the chinchillas and all the other cases that
10 come along in the Howey chain. The utility doesn't matter.

11 Judge Selya says the fact that it's a game doesn't
12 matter both in disqualifying it as a securities transaction
13 and in whether or not there's a reasonable expectation of
14 profits. Because that's what the SG defendants said. They
15 said this was a game. How could anybody have expected
16 profits? And Judge Selya said, well, pretty much because you
17 told them to expect profits, and that's what LBRY did here.

18 THE COURT: Okay. And you will look at your brief
19 to see the specific instances.

20 Can you just refresh my memory? I'm remembering
21 from the briefs that in fact there were several instances in
22 which LBRY did make substantial sales of LBCs. I mentioned
23 the investment club was one of them. There were others
24 according to you, right?

25 MR. JONES: Yes, your Honor.

1 So the investment club sales -- there are several
2 of those sales. I believe there are four. I could be wrong
3 and there's five. I think there's four. They were two
4 different investment clubs run by the same investment house, a
5 place called Flipside Crypto. Overall 1.1 million LBC, for a
6 value of around that time \$260,000, were sold to what was
7 advertised as a small group of influential people.

8 It is not credible in the -- and this is what the
9 cases say, too. Look at the actual transaction to see what
10 the economic realities are. Part of the economic realities
11 are how many, how much, and what would it have taken you to
12 actually consume those millions and millions of videos.

13 First of all, your Honor, most of the videos are
14 free to watch. Most of them cost a tenth of an LBC to publish
15 unless you're publishing it from YouTube, in which case LBRY
16 pays it for you. Tipping is optional. And this process of
17 what's called staking, which is supporting a channel by
18 putting down your LBC, is a nonconsumptive use. You can take
19 all your LBC back. It's not even really something we need to
20 worry about.

21 So when Flipside Crypto comes along in 2017 and
22 2018 and buys 1.1 million of these, says they're going to put
23 them in cold storage, which right there you know is not going
24 to be a consumptive use because --

25 THE COURT: Sorry. The names are mixing up. Who

1 is that?

2 MR. JONES: That's Flipside Crypto. They are the
3 investment clubs.

4 THE COURT: They were the investment clubs?

5 MR. JONES: Yes, your Honor.

6 Right there when they say we're going to put them
7 in cold storage, cases like Telegram say, well, that's part of
8 the economic reality you look at. The fact that you're buying
9 it to put in cold storage means that -- no one would buy
10 something that they wanted to use and then voluntarily agree
11 to put it away for a year for no reason. They're putting it
12 in cold storage.

13 The same thing with Pillar. Pillar is the venture
14 capital investor that originally just gives money. They are
15 purely a venture capital investor at the beginning, and then
16 as time goes on, it's 2018, they say we've done a lot of other
17 valuable things for you. We want to negotiate that you give
18 us LBC for them. They make a contract. A million LBC is
19 promised in that contract. It's got a lock-up period.

20 THE COURT: I wanted to ask you -- so there is a
21 lock-up period?

22 MR. JONES: There is on that, your Honor.

23 THE COURT: Okay.

24 MR. JONES: Now, my friends at LBRY say, well, they
25 never took possession of them.

1 THE COURT: What does that mean, they never took
2 possession of them?

3 MR. JONES: Apparently, they never transferred them
4 from LBRY's wallet to their own wallet.

5 THE COURT: Did they give -- so what did they --
6 what was their consideration for the transaction?

7 MR. JONES: In the agreement it's specifically
8 cited as a change in loan terms essentially, a change in debt
9 terms.

10 THE COURT: So there's some kind of debt security
11 that evidences the Pillar contribution?

12 MR. JONES: I think -- the second part, absolutely,
13 your Honor, the tokens were to recognize the Pillar
14 contribution. The testimony states that. I don't even know
15 if you have that testimony, your Honor, but the testimony does
16 state that.

17 The first part was -- I don't want to say it was
18 for debt. It was in consideration of changing the terms of
19 prior debt --

20 THE COURT: Okay.

21 MR. JONES: -- is my understanding. But the
22 testimony is also the LBRY folks and the Pillar folks both
23 thought that it was also coming from the fact that Pillar had
24 contributed services and advice and things like that. Now,
25 that's not specified in the agreement as we've put into the

1 record, but that's what the testimony is.

2 THE COURT: But Pillar -- whatever this agreement
3 was, there never was an actual transfer from the LBC -- or the
4 LBRY wallet to the Pillar wallet?

5 MR. JONES: Let me answer that in two ways, your
6 Honor.

7 As far as we know, there was never an electronic
8 transfer from one wallet to the other.

9 On the other hand, Pillar gets audited. The
10 auditor says to LBRY, confirm that there are 2 million LBC
11 that are possessed by Pillar that you owe to them. LBRY says
12 yes. Pillar says yes. It goes in their audit. It's listed
13 as an asset on their books.

14 THE COURT: It could be an off-chain transaction.

15 MR. JONES: Well, your Honor --

16 THE COURT: There's a right to recover that
17 remains, right? So Pillar could sue LBRY and say you've
18 agreed to give me -- in exchange for agreements about debt or
19 so forth, we had some kind of a contract, and they could
20 execute on it you're saying.

21 MR. JONES: And I don't think either side disputes
22 the fact that if Pillar said an hour from now I'm taking my
23 LBC now, that LBRY wouldn't absolutely just give it to them.
24 I think they're willing to give it to them, I think they know
25 they have to give it to them, and they've stated on the audit

1 that they are Pillar's LBC that they're holding onto -- that
2 LBRY is holding onto for them.

3 I think the details of that are less significant
4 than the economic reality of that transaction, which is 2
5 million LBC sold, you know, for valuable consideration and put
6 into a lock-up period, which means that absolutely it was not
7 for consumptive intent.

8 There are others, your Honor. The sales on the
9 platform go from 2017 through 2021 with a little break in the
10 middle. There's also market making during that time, and we
11 think the market making is significant. Why? Because in
12 addition to what LBRY has said is going to happen with these,
13 they are actually taking affirmative steps and paying for
14 services to create and stabilize a market in LBC.

15 Now, if you're buying four LBC to watch some
16 videos, you're not destabilizing a market. If you're buying
17 or selling 10,000, 100,000, a million, there's market making
18 that can stabilize a market in that point.

19 And in fact we know those are the levels because
20 there were two accounts that the market maker controlled, one
21 in the name of Mr. Kauffman and one in the name of another
22 executive, and those accounts together traded 7.4 billion LBC
23 over the time period June 2020 to March --

24 THE COURT: Let me just make sure I understand your
25 argument.

1 MR. JONES: Yes, your Honor.

2 THE COURT: And then we're going to have to take a
3 break in a minute for my reporter.

4 MR. JONES: Yes, your Honor.

5 THE COURT: You're saying I can infer from the fact
6 that LBRY was engaged, actively engaged in market making
7 activities for LBC that they understood that this would be a
8 substantial investment use of LBC and they needed to have
9 market making to prevent wild swings in the value of LBC
10 whenever one of these holders of a substantial amount decides
11 to dump it. If it was just people who are using LBC for
12 consumptive purposes, it would sort of gurgle along at a
13 steady and hopefully significantly increasing but not a need
14 to have market making you would say?

15 MR. JONES: That is our argument, your Honor. Yes.

16 THE COURT: I suppose their argument would be if we
17 want LBC to be valuable at all, we've got to have viable
18 markets, and if there aren't viable markets, we can't --
19 nobody is going to hold an LBC for any purpose because they
20 can't -- it's completely nonliquid.

21 MR. JONES: Well, that may be what they say, but
22 you can certainly have LBC in a Pocketful of Quarters kind of
23 way that you wouldn't have that concern. It's only when you
24 have -- people want to have these and hold onto them and have
25 the value go up in the future that you're concerned about

1 that.

2 THE COURT: Let's stop in a minute.

3 MR. JONES: Yes, your Honor.

4 THE COURT: I want to ask this one question. Just
5 so people know, I have another thing at 3:30 that I've got to
6 do. We'll take a break. We'll come back and finish your
7 argument, give LBRY a brief chance to respond. Then LBRY will
8 present on its fair notice argument, give you a brief chance
9 to respond. I've got to wrap up by 3:30.

10 So if you accept the view, as I think many people
11 do, that blockchains like the one LBRY operates have great
12 potential utility for our society -- and we want to encourage
13 people to use things like blockchains at least under certain
14 circumstances. Obviously, people have different views about
15 it consumes too much energy, it's not good for society, but
16 there are a lot of people that think they have great economic
17 utility and real potential.

18 It seems an essential part of an operation of
19 blockchain that you have to incentivize people that validate
20 blocks of the blockchain, and the way in which that's been
21 traditionally done is through a digital asset.

22 Is there in the SEC's mind a way in which LBRY
23 could operate the LBRY blockchain using LBC as a digital asset
24 that would not qualify LBC as a digital asset -- as a
25 security? Excuse me.

1 MR. JONES: Your Honor, I want to be very careful
2 for this answer.

3 THE COURT: I understand.

4 MR. JONES: I am not a commissioner appointed by
5 the senate. I am not a policy maker. I am a lowly trial
6 attorney, enforcement attorney who's in charge of enforcing
7 the law as it stands now.

8 THE COURT: Well, let me just suggest -- because
9 I'm none of those things. I'm not even a lowly SEC attorney.
10 I'm lower than that.

11 Couldn't they operate as Pocketful of Quarters and
12 use LBC in the same way that a token in Pocketful of Quarters
13 was used which generated an SEC no-action letter?

14 MR. JONES: Your Honor, to answer as honestly as I
15 can without making any policy for the Commission, I believe
16 there are probably several ways that all are focused on the
17 Howey test. And if you can disqualify yourself from a certain
18 part of the Howey test then, all things being equal, you're
19 probably operating in a way that would be allowed. The
20 Pocketful of Quarters no-action letter. The no-action letters
21 the Commission has issued.

22 If you can make it so there's not an expectation of
23 profits, if there's no common enterprise, that's a way that,
24 you know, that's talked about.

25 If there's no reasonable efforts of others, if

1 you're not putting in any efforts, as your Honor was talking
2 about before, perhaps, and without binding the Commission in
3 any way, perhaps all of those would be ways that you could do
4 a blockchain program without violating the Howey test.

5 But from my perspective, your Honor, I have the
6 Howey test, and I can see what LBRY has done.

7 THE COURT: Are there ways if you conclude that
8 it's -- again, you can't bind the SEC.

9 MR. JONES: Correct.

10 THE COURT: I understand. I'm just trying to gain
11 this out.

12 If it did qualify as a security -- as we all know,
13 there are vast, vast quantities of transactions that are
14 securities transactions that are exempt from registration
15 requirements. Indeed, the private placement market is bigger
16 than the registered market so there are more trillions of
17 dollars exchanged in the private market than the public
18 market.

19 Would someone like LBRY be able to qualify under
20 one of the exemptions, the many exemptions that exist?

21 MR. JONES: Your Honor, I would presume that if
22 you're -- I don't want to say that LBRY could because LBRY has
23 done certain things.

24 If you're a company who's putting out tokens and
25 you qualify for the exemptions, there's nothing in my

1 understanding that says because you're a blockchain company
2 you don't qualify for the exemptions.

3 If you're going to make a general solicitation,
4 you're going to have a hard time qualifying for the
5 exemptions.

6 THE COURT: Well, there are small dollar
7 solicitations. There are interstate solicitations.

8 MR. JONES: Yes, your Honor.

9 THE COURT: You know, there are exemptions --

10 MR. JONES: Absolutely.

11 THE COURT: -- which are gigantic in number.

12 Okay. I just was curious about that. I'm not
13 trying to bind the SEC. I just was interested in the
14 counterfactual -- if we deem blockchain to be useful and we
15 deem digital assets to be important to function as a
16 blockchain and we don't want people to have to engage in the
17 burden of registration, are there ways that this could be done
18 that wouldn't subject the blockchain creator to the obligation
19 to register.

20 It seems to me that there are, but I don't know --
21 one thing that would not be able to do, which is a company
22 that wants to rely on the growth and the value of its holding
23 of its coin as the means to finance the growth of the company.

24 MR. JONES: Right.

25 THE COURT: It's very hard to do that and have it

1 not be a Howey investment contract under your client's view,
2 right?

3 MR. JONES: And so, your Honor, that's exactly what
4 LBRY did here. In fact, they put out a whole post, it's
5 Exhibit 43, about how there's a whole new way of doing
6 business, and we can create these tokens. We don't have to
7 exploit our customers because we can sell these tokens because
8 they'll go up in value over time, and that's how we'll fund
9 and build our business.

10 So that latter part, the part where you said it's
11 very hard for it not to be an investment contract, that's what
12 LBRY did.

13 But in my personal opinion, I think which may be
14 what the Court is also expressing, there are ways to not run
15 afoul of the Howey test and still run a blockchain.

16 THE COURT: Yeah. That's what I'm just wondering,
17 you know, because it does seem that there are very important
18 valuable uses of blockchain technology and there would be
19 seemingly ways to run a blockchain successfully without the
20 digital asset being a security, like Pocketful of Quarters,
21 but it would be hard to do that if your business model is we
22 don't need large amounts of venture capital. We don't need to
23 charge people for stuff. We will just build a blockchain with
24 a digital asset that will increase in value in the future as
25 we build out and succeed with the blockchain because that's

1 quintessentially people who -- it goes up in value because
2 people want to buy it. People want to buy it because it's
3 going to become more valuable in the future because the
4 company builds it up. That's sort of quintessentially Howey.
5 That's your position?

6 MR. JONES: That is, your Honor.

7 THE COURT: All right.

8 Again, take a short break. As soon as my court
9 reporter is ready, we'll come back, hear LBRY's response,
10 LBRY's argument about fair notice, your response, and then
11 we'll wrap up, okay?

12 MR. JONES: Thank you, your Honor.

13 (RECESS)

14 THE COURT: So just to anticipate something I
15 assume LBRY is going to ask you, I want your answer first.

16 You place great weight on things LBRY said in
17 connection with or loosely or more directly related to
18 offerings of LBC. LBRY says, look, that's one tiny fraction
19 of all the things we said about LBC and our app, and we
20 actually said things like don't look at it as an investment,
21 you know, and they swamp those few things that you point to.
22 What's your response to that?

23 MR. JONES: A couple of responses there, your
24 Honor.

25 First of all, they don't swamp it with everything

1 they said about LBC. They swamp it with everything they've
2 said about everything. New functionality. Hey, we got a new
3 video. This person is joining our platform. We're a bunch of
4 cool guys. This is the guy that we created that we write a
5 pen name under.

6 It's not all the things we said about LBC. This is
7 a small fraction. The things that the Commission have cited
8 that they said about LBC or the things that they've said about
9 LBC, that's -- I mean, we put in a lot of stuff because that's
10 what they've said.

11 And you won't find anywhere in the record submitted
12 by LBRY except one time where they said don't expect a profit.
13 Don't think this is going to go up over the long-term. We're
14 not working on this. You will not make a -- this will not go
15 up in value. They say nothing like that except one time.

16 The one time they say it is when they're selling
17 hundreds of thousands of tokens to Flipside Crypto, the
18 investment club that you and I were talking about before, your
19 Honor. And they say as an afterthought, after the deal is
20 consumed, oh, by the way, we are very conscious of the
21 securities laws. This is not for investment. This is for use
22 on the platform. Not credible. In fact, perhaps proving the
23 opposite in the fact that they felt that --

24 THE COURT: That kind of disclaimer you would say
25 is of really no value. It's just designed to show the

1 awareness that this is potentially an offering of security?

2 MR. JONES: Correct, your Honor.

3 So I think Mr. Miller is right when he says you
4 look at the promotional materials. You know, when they talked
5 about LBC, they talked about it in the way that the Commission
6 has presented with its many exhibits, and LBRY has not
7 presented any exhibits that show that they talked about it in
8 a different way.

9 And so, yes, they may have said 8,000 things, but
10 the test is not about how verbose the defendant is, as we say
11 in our brief, or reticent. The question is when they talk
12 about LBC -- and in many of the cases there's two or three
13 documents.

14 THE COURT: Let me ask you about reticence. What's
15 the oil well case, the Supreme Court's oil well case about
16 leases of the land in --

17 MR. JONES: It's Joiner, your Honor.

18 THE COURT: Joiner.

19 MR. JONES: Yes.

20 THE COURT: What the Court in Joiner said was this
21 might well be a different case had they not engaged in any
22 kind of promotional statements.

23 Do you think a complete absence of promotional
24 statements would be sufficient for a company like this?

25 MR. JONES: I don't, your Honor.

1 And, first, I don't think I necessarily agree with
2 you exactly what the Court says in Joiner.

3 THE COURT: I'm trying to do it from memory.

4 MR. JONES: In Joiner -- and Judge Selya talks
5 about this actually. In Joiner they say if you had never said
6 that this exploratory drilling part of the deal could render
7 you some profit, right, they say the exploratory drilling part
8 of the deal is the part that drives the expectation of
9 profits. Otherwise, I think they call it a leasehold interest
10 in what is otherwise a, you know, possibly oil-filled,
11 probably dry piece of land.

12 So I think the point that's being made in Joiner
13 there is -- you know, normally, like in Forman, you might have
14 just a leasehold interest, but once you put an exploratory
15 drilling part on it that actually gives it the value, the
16 economic reality of that transaction is that there's an
17 expectation of profits which we can see by the fact that you
18 talked about it and highlighted it. I don't think, your
19 Honor, if they hadn't talked about it but still had it, that
20 the Joiner Court might have said, well, there is no
21 expectation of profits here.

22 And the reason I say that, your Honor, is because
23 the courts in analyzing this, whether it's Joiner or SG or
24 Forman or Telegram or Kik, they look at not just what is said,
25 and I think it's inappropriate to look at just what it said.

1 They look at the structure of the transaction.

2 Here LBRY creates these things. It holds back 400
3 million. It starts to sell them out in the world. And then
4 it makes statements.

5 But the whole structure of the transaction in the
6 first place, which is we are going to fund our business -- our
7 business model, as you said, is -- and it was admitted as
8 testimony and submitted as part of this record. All of the
9 money to build LBRY --

10 THE COURT: So your point is -- at least your
11 perspective, again not binding the SEC, but you're saying even
12 if they had been completely silent but had structured the
13 transactions the way they did, engaged in the transactions,
14 held back the 400,000, whatever, million, whatever --

15 MR. JONES: Yes, your Honor.

16 THE COURT: -- all of that, that would have been
17 enough. You don't need these statements in this case to
18 satisfy Howey.

19 MR. JONES: I believe that's right, your Honor,
20 because I don't believe that the securities laws permit you to
21 put out what is a security in an economic reality and stay
22 quiet and evade the securities laws. That's what I have to
23 look out for here, that there's some loophole created that,
24 hey, you know, we never said this was going up, but everything
25 we did showed that that's what we thought and the whole part

1 of the transaction that that's how it worked, and it did.

2 I want to say one more thing, your Honor, before I
3 sit down.

4 THE COURT: One more thing, and then I've got to
5 let LBRY have a turn.

6 MR. JONES: Of course, our Honor.

7 You seem to think that the Commission was buying
8 into this off-chain/on-chain ratio. We think that's bunk.
9 The way that it's presented --

10 THE COURT: I thought you were making arguments
11 based on on-chain/off-chain ratio.

12 MR. JONES: We're making I think rebuttal arguments
13 based on if you actually look at the data, here's what it is,
14 your Honor, and in fact we've rebutted it in our --

15 THE COURT: So you agree with me that it doesn't
16 necessarily tell you which uses are consumptive or not?

17 MR. JONES: No, your Honor.

18 The on-chain transaction is extraordinarily
19 problematic. We've outline that in our Daubert motion we just
20 submitted to you.

21 THE COURT: I have not seen it.

22 MR. JONES: Of course, your Honor. There's more
23 than enough here.

24 But not only is it bunk in the way that it's done,
25 not only is it not a reliable proxy for consumptive use, it's

1 not a -- even if it was, it's not a workable test. You can't
2 have the securities laws basically say, well, you don't know
3 whether it's a security until five years down the line when
4 you see if enough of these people bought it and not enough of
5 those people.

6 THE COURT: No. I agree that it couldn't work as a
7 test in and of itself. The issue is, is it a relevant -- can
8 it be a relevant factor at all in consideration, and I think
9 this is where you and LBRY may disagree. I think they say
10 evidence of what subjective intent of acquirers of a digital
11 asset, evidence of that is potentially useful, and so if we
12 were able to show here in a perfect world 100 percent of the
13 acquirers of LBC acquired it for consumptive use and we were
14 able to prove that conclusively, that they would say that's
15 very, very strong evidence that -- just like people who bought
16 the apartments wanted to live there and not the stock, people
17 who bought LBC and in fact used it entirely for consumptive
18 purposes wanted to use it for consumptive purposes, not for
19 investment. So that's why I think at least in theory in
20 extreme cases it might be relevant. It's not dispositive.
21 I'm just saying it may be a factor that I can consider.

22 MR. JONES: I understand, your Honor, but I think
23 the key part of what you said at the end there was that they
24 bought it for consumptive purposes and not for investment
25 purposes.

1 THE COURT: Right.

2 MR. JONES: Once you're in for investment purposes,
3 even for part of it, even by some people, even, you know, a
4 fraction of those people, you're in securities land.

5 THE COURT: Yeah, but if you're buying -- people
6 buy houses. Do you live in a house you own?

7 MR. JONES: I do, your Honor.

8 THE COURT: If you have, you probably think, you
9 know what, rather than rent a house, I'm going to buy a house.

10 MR. JONES: Yes.

11 THE COURT: Because over time I'm going to make
12 some appreciation in the value of the house or maybe it's a
13 hedge against inflation or something else. It's primarily I
14 want to live in it, you know, but houses are, like under the
15 family resemblance test or something, they wouldn't be
16 investment contracts necessarily, but the point is that there
17 are things that people acquire both because they have some
18 investment value but principally because they have some
19 consumptive value which are not going to satisfy the Howey
20 test.

21 MR. JONES: Absolutely, your Honor. And I would
22 say in most of those circumstances it's going to fail on a
23 different part of the Howey test before you even get to
24 expectation of profits. Your house is not a common
25 enterprise.

1 THE COURT: Right.

2 MR. JONES: And to the extent it goes up in profit,
3 it's because possibly you improve it.

4 So I would say there absolutely are, your Honor,
5 there are Beanie Babies in the world, but they're not LBC.

6 Thank you, your Honor.

7 THE COURT: All right. So let me hear from LBRY
8 briefly in response to what you've heard, and then your
9 argument on fair notice, and then I can only give you about
10 ten minutes at most and then I'll get a brief response from
11 the SEC, and then we'll wrap up.

12 MR. MILLER: Thank you, your Honor.

13 We completely disagree with the SEC's analysis here
14 that simply running an application on a blockchain where an
15 entity owns those tokens turns those tokens into a security.
16 That is not the test.

17 THE COURT: Well, I don't think it's the test, but
18 I also don't think that's what they're saying.

19 MR. MILLER: Well, we believe -- let me change a
20 little point here.

21 Your Honor has been focusing on what type of
22 promotional material is enough. What is enough?

23 We think the SG case in using the word the
24 principal attraction, we believe that the Price case which
25 said, used the word primarily, and we believe that -- and

1 that's an Eleventh Circuit case, we believe the Second
2 Circuit's case in SEC versus Aqua-Sonic where they said the
3 overall emphasis, those words, particularly in the First
4 Circuit SG case, mean something. We think they were put there
5 for a reason.

6 Next point, your Honor.

7 THE COURT: I mean, I'm going to have to think more
8 about that. I do think it's a point worth considering, but I
9 don't think it involves a mechanical counting up of the number
10 of investors and their subjective statements as to what they
11 acquired the asset for. That would be an impossible to
12 administer test and shouldn't really be the focus, but your
13 point is not that because you agree that it's a reasonable
14 investor test and you agree that it's economic reality and you
15 agree that it's totality of circumstances. You're just saying
16 subjective intent can be relevant and this is evidence of
17 subjective intent, and when there's an undeniable, substantial
18 in your view, consumptive use, the SEC isn't really able to
19 prove that using the reasonable objective purchaser standard
20 that this is an acquisition or an offer because of expectation
21 of profit?

22 MR. MILLER: That's correct. And I think although
23 we believe that the evidence presented, which when looked at
24 by a reasonable investor here, would suggest that LBRY is not
25 promoting it for investment.

1 We do recognize that there's a counterargument here
2 and question whether either side would be -- whether it would
3 be appropriate for the Court to rule on summary judgment for
4 either side given the arguments.

5 THE COURT: I'm either going to rule on
6 cross-motions or I'm going to hold a trial and rule. It's not
7 like we're going to have a jury decide this case, right? I
8 assume -- I haven't looked, but you haven't made some demand
9 for a jury, which would be very unusual.

10 I'm just not sure what else I would uncover at
11 trial that I don't already have in front of me. I mean, it
12 seems like you've both done a good job of putting together the
13 core arguments on your respective positions. But in any
14 event, I hear your point on that.

15 MR. MILLER: And lastly, your Honor, if the SEC is
16 right about how they interpret this, and that is go look at an
17 application on a blockchain and look what they say about the
18 token, and when you look at what they say about the token, it
19 talks about -- what is it talking about? It's talking about
20 the underlying blockchain and the fact that they're building a
21 protocol, and because they own tokens in that blockchain that
22 makes it a security.

23 I think that is turning the entire Howey test
24 upside down. It's then converting it into I think a
25 subjective test, not a reasonable investor test that is

1 looking at promotional materials.

2 Again, I would argue if LBRY -- if the LBRY credits
3 are tokens, then thousands of companies that run on Ethereum
4 platform, that use Bitcoin, they're all going to be deemed to
5 be security.

6 THE COURT: Yeah, that's a bit of an overstatement.
7 I mean something like Bitcoin that doesn't have an entity, a
8 business that's trying to build out the Bitcoin blockchain and
9 isn't offering anything to anybody, it's completely different.

10 MR. MILLER: It does have -- Bitcoin has been
11 forked many times. Not many times but a few times. And who's
12 done that? The members. The people who run those notes.
13 Just like LBRY, just like Ethereum, those are members who make
14 determinations of we should do this in the software. It's
15 more advantageous for all the users. And so if people adopt
16 it, then it's forked.

17 So there's nothing different between Bitcoin, which
18 is the transfer of value, and LBRY. It's a transfer of value.
19 That's all it is. It's -- can people believe that it's an
20 investment? Certainly. But what is -- and it goes back to
21 what did LBRY do to promote this. That's what you need to
22 look at. I think the courts are saying look at the
23 promotional material. And when you look at the promotional
24 material, you don't have what the SEC has alleged in SEC
25 versus Telegram, SEC versus Kik. You don't have any of these

1 issues of a private place memoranda, what someone normally
2 would think of.

3 I think, your Honor, we're struggling with dual
4 purposes. The reason you don't have those cases is because
5 the government usually passes on those cases because they
6 recognize, well, people can disagree on whether it's
7 investment or whether it's use. We're not going to go
8 prosecute this case.

9 For some reason they made this a case, and we think
10 under Howey, its progeny, the First Circuit case law of SG,
11 this does not constitute -- LBRY credits do not constitute
12 securities.

13 THE COURT: Okay. Thank you. Did you want to say
14 anything more on the fair notice argument? You raised it in
15 your brief. I think I understand it, but if there's anything
16 you want to add on that.

17 MR. MILLER: No. Nothing further, your Honor.

18 THE COURT: All right.

19 Any last comment from you before we wrap up?

20 MR. Jones: No, your Honor. We absolutely believe
21 this is ripe for summary judgment, and we think the case law
22 supports you deciding it as a question of law.

23 THE COURT: Okay. I'll take the matter under
24 advisement. I think it's been well-argued. The oral argument
25 has been helpful to me. It's a significant issue. I want to

1 make sure I devote substantial time to it. It may be 30 to 60
2 days before I get out a ruling on it.

3 I'm going to stay LBRY's need to respond to the
4 Daubert motion because it isn't going to take -- I'm not going
5 to take that into account when ruling on this matter, and I'm
6 not considering the supplemental expert disclosure either. So
7 you don't have to answer the Daubert motion. I'm not going to
8 look at it. If you want to answer it, you can, but I just
9 don't want to make you work unnecessarily. I tend to take
10 those motions before trial anyway. And before I determine
11 there's a need for trial here, I don't think there's a need in
12 ruling on the Daubert motion.

13 So the time for you to respond to that is stayed
14 until further order of the Court.

15 If I determine that there's a triable matter left
16 at the end of this, I'll schedule a further status conference
17 to discuss any remaining matters that have to be done. So I
18 wouldn't expect the parties to be either engaging in
19 substantial additional discovery now or doing anything, filing
20 things with the Court. I have this briefed. I'm ready to go.
21 Give me my time to rule on it. Then we'll revisit if
22 necessary.

23 Is that acceptable to you?

24 MR. JONES: It's absolutely acceptable, your Honor.

25 Just as a matter of clarification, when we asked to

1 have the trial pushed to October 4th there were automatic
2 pretrial submission dates.

3 THE COURT: Everything is stayed until further
4 order of the Court.

5 MR. JONES: Thank you, your Honor.

6 THE COURT: I have to decide whether there's a
7 triable case here. I don't want people to spend money on
8 things that might not be necessary.

9 MR. JONES: We appreciate that.

10 THE COURT: I recognize how expensive litigation
11 is. It's now in my hands for a while. If there's something
12 that survives after this, we'll meet again and set up new
13 deadlines and all of that, okay?

14 It is important. I want to get it done. I'm going
15 to try to get it done expeditiously. I hope by the end of
16 August, but certainly by the end of September I'll have
17 something, and then we can chat, okay?

18 All right. Thank you. That concludes the hearing.

19 MR. MILLER: Thank you, your Honor.

20 MR. JONES: Thank you, your Honor.

21 (Conclusion of hearing at 3:15 p.m.)
22
23
24
25

C E R T I F I C A T E

I, Susan M. Bateman, do hereby certify that the foregoing transcript is a true and accurate transcription of the within proceedings, to the best of my knowledge, skill, ability and belief.

Submitted: 7-31-22

/s/ Susan M. Bateman
SUSAN M. BATEMAN, RPR, CRR